

AMENDED IN ASSEMBLY MARCH 26, 2015

CALIFORNIA LEGISLATURE—2015–16 REGULAR SESSION

## ASSEMBLY BILL

No. 922

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**Introduced by Assembly Member Gallagher**

February 26, 2015

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~~An act relating to economic development.~~ *An act to amend Section 6377.1 of the Revenue and Taxation Code, relating to taxation, to take effect immediately, tax levy.*

### LEGISLATIVE COUNSEL'S DIGEST

AB 922, as amended, Gallagher. ~~Economic development.~~ *Sales and use taxes: exemption manufacturing.*

*Existing sales and use tax laws impose taxes on retailers measured by the gross receipts from the sale of tangible personal property sold at retail in this state, or on the storage, use, or other consumption in this state of tangible personal property purchased from a retailer for storage, use, or other consumption in this state, and provides various exemptions from those taxes.*

*Existing law exempts from those taxes, on and after July 1, 2014, and before January 1, 2022, the gross receipts from the sale of, and the storage, use, or other consumption of, qualified tangible personal property purchased by a qualified person for use primarily in manufacturing, processing, refining, fabricating, or recycling of property, as specified; qualified tangible personal property purchased for use by a contractor for specified purposes, as provided; and qualified tangible personal property purchased for use by a qualified person to be used primarily in research and development, as provided. Existing law defines a "qualified person" to be a person that is primarily engaged in specified lines of business.*

*Existing law specifies that this exemption does not apply to local sales and use taxes, transactions and use taxes, and specified state taxes from which revenues are deposited into the Local Public Safety Fund, the Education Protection Account, the Local Revenue Fund, the Fiscal Recovery Fund, or the Local Revenue Fund 2011.*

*This bill would delete that repeal date, thereby extending the application of the exemption indefinitely. The bill, on or after January 1, 2023, would limit the exemption to a qualified person that is located in a county, city and county, or metropolitan statistical area that had an unemployment rate of 10% or more in the previous calendar quarter.*

*This bill would take effect immediately as a tax levy.*

~~Existing law provides for various economic development programs that foster community sustainability and for community and economic development initiatives throughout the state.~~

~~This bill would express the intent of the Legislature to develop a new economic program that would operate in areas with high unemployment.~~

Vote: majority. Appropriation: no. Fiscal committee: ~~no~~ yes.  
State-mandated local program: no.

*The people of the State of California do enact as follows:*

1     SECTION 1. Section 6377.1 of the Revenue and Taxation Code  
2     is amended to read:

3     6377.1. (a) Except as provided in subdivision (e), on or after  
4     July 1, 2014, ~~and before July 1, 2022~~, there are exempted from the  
5     taxes imposed by this part the gross receipts from the sale of, and  
6     the storage, use, or other consumption in this state of, any of the  
7     following:

8     (1) Qualified tangible personal property purchased for use by  
9     a qualified person to be used primarily in any stage of the  
10    manufacturing, processing, refining, fabricating, or recycling of  
11    tangible personal property, beginning at the point any raw materials  
12    are received by the qualified person and introduced into the process  
13    and ending at the point at which the manufacturing, processing,  
14    refining, fabricating, or recycling has altered tangible personal  
15    property to its completed form, including packaging, if required.

16    (2) Qualified tangible personal property purchased for use by  
17    a qualified person to be used primarily in research and  
18    development.

1 (3) Qualified tangible personal property purchased for use by  
2 a qualified person to be used primarily to maintain, repair, measure,  
3 or test any qualified tangible personal property described in  
4 paragraph (1) or (2).

5 (4) Qualified tangible personal property purchased for use by  
6 a contractor purchasing that property for use in the performance  
7 of a construction contract for the qualified person, that will use  
8 that property as an integral part of the manufacturing, processing,  
9 refining, fabricating, or recycling process, or as a research or  
10 storage facility for use in connection with those processes.

11 (b) For purposes of this section:

12 (1) "Fabricating" means to make, build, create, produce, or  
13 assemble components or tangible personal property to work in a  
14 new or different manner.

15 (2) "Manufacturing" means the activity of converting or  
16 conditioning tangible personal property by changing the form,  
17 composition, quality, or character of the property for ultimate sale  
18 at retail or use in the manufacturing of a product to be ultimately  
19 sold at retail. Manufacturing includes any improvements to tangible  
20 personal property that result in a greater service life or greater  
21 functionality than that of the original property.

22 (3) "Primarily" means 50 percent or more of the time.

23 (4) "Process" means the period beginning at the point at which  
24 any raw materials are received by the qualified person and  
25 introduced into the manufacturing, processing, refining, fabricating,  
26 or recycling activity of the qualified person and ending at the point  
27 at which the manufacturing, processing, refining, fabricating, or  
28 recycling activity of the qualified person has altered tangible  
29 personal property to its completed form, including packaging, if  
30 required. Raw materials shall be considered to have been  
31 introduced into the process when the raw materials are stored on  
32 the same premises where the qualified person's manufacturing,  
33 processing, refining, fabricating, or recycling activity is conducted.  
34 Raw materials that are stored on premises other than where the  
35 qualified person's manufacturing, processing, refining, fabricating,  
36 or recycling activity is conducted shall not be considered to have  
37 been introduced into the manufacturing, processing, refining,  
38 fabricating, or recycling process.

1 (5) “Processing” means the physical application of the materials  
2 and labor necessary to modify or change the characteristics of  
3 tangible personal property.

4 (6) (A) (i) “Qualified person” means a person that is primarily  
5 engaged in those lines of business described in Codes 3111 to  
6 3399, inclusive, 541711, or 541712 of the North American Industry  
7 Classification System (NAICS) published by the United States  
8 Office of Management and Budget (OMB), 2012 edition.

9 (ii) *On or after January 1, 2023, “qualified person” means a*  
10 *qualified person, as defined in clause (i), that is located in a county,*  
11 *city and county, or metropolitan statistical area that had an*  
12 *unemployment rate of 10 percent or more in the previous calendar*  
13 *quarter.*

14 (B) Notwithstanding subparagraph (A), “qualified person” shall  
15 not include either of the following:

16 (i) An apportioning trade or business that is required to apportion  
17 its business income pursuant to subdivision (b) of Section 25128.

18 (ii) A trade or business conducted wholly within this state that  
19 would be required to apportion its business income pursuant to  
20 subdivision (b) of Section 25128 if it were subject to apportionment  
21 pursuant to Section 25101.

22 (7) (A) “Qualified tangible personal property” includes, but is  
23 not limited to, all of the following:

24 (i) Machinery and equipment, including component parts and  
25 contrivances such as belts, shafts, moving parts, and operating  
26 structures.

27 (ii) Equipment or devices used or required to operate, control,  
28 regulate, or maintain the machinery, including, but not limited to,  
29 computers, data-processing equipment, and computer software,  
30 together with all repair and replacement parts with a useful life of  
31 one or more years therefor, whether purchased separately or in  
32 conjunction with a complete machine and regardless of whether  
33 the machine or component parts are assembled by the qualified  
34 person or another party.

35 (iii) Tangible personal property used in pollution control that  
36 meets standards established by this state or any local or regional  
37 governmental agency within this state.

38 (iv) Special purpose buildings and foundations used as an  
39 integral part of the manufacturing, processing, refining, fabricating,  
40 or recycling process, or that constitute a research or storage facility

1 used during those processes. Buildings used solely for warehousing  
2 purposes after completion of those processes are not included.

3 (B) “Qualified tangible personal property” shall not include any  
4 of the following:

5 (i) Consumables with a useful life of less than one year.

6 (ii) Furniture, inventory, and equipment used in the extraction  
7 process, or equipment used to store finished products that have  
8 completed the manufacturing, processing, refining, fabricating, or  
9 recycling process.

10 (iii) Tangible personal property used primarily in administration,  
11 general management, or marketing.

12 (8) “Refining” means the process of converting a natural  
13 resource to an intermediate or finished product.

14 (9) “Research and development” means those activities that are  
15 described in Section 174 of the Internal Revenue Code or in any  
16 regulations thereunder.

17 (10) “Useful life” for tangible personal property that is treated  
18 as having a useful life of one or more years for state income or  
19 franchise tax purposes shall be deemed to have a useful life of one  
20 or more years for purposes of this section. “Useful life” for tangible  
21 personal property that is treated as having a useful life of less than  
22 one year for state income or franchise tax purposes shall be deemed  
23 to have a useful life of less than one year for purposes of this  
24 section.

25 (c) An exemption shall not be allowed under this section unless  
26 the purchaser furnishes the retailer with an exemption certificate,  
27 completed in accordance with any instructions or regulations as  
28 the board may prescribe, and the retailer retains the exemption  
29 certificate in its records and furnishes it to the board upon request.

30 (d) (1) Notwithstanding the Bradley-Burns Uniform Local  
31 Sales and Use Tax Law (Part 1.5 (commencing with Section 7200))  
32 and the Transactions and Use Tax Law (Part 1.6 (commencing  
33 with Section 7251)), the exemption established by this section  
34 shall not apply with respect to any tax levied by a county, city, or  
35 district pursuant to, or in accordance with, either of those laws.

36 (2) Notwithstanding subdivision (a), the exemption established  
37 by this section shall not apply with respect to any tax levied  
38 pursuant to Section 6051.2, 6051.5, 6201.2, or 6201.5, pursuant  
39 to Section 35 of Article XIII of the California Constitution, or any  
40 tax levied pursuant to Section 6051 or 6201 that is deposited in

1 the State Treasury to the credit of the Local Revenue Fund 2011  
2 pursuant to Section 6051.15 or 6201.15.

3 (e) (1) The exemption provided by this section shall not apply  
4 to either of the following:

5 (A) Any tangible personal property purchased during any  
6 calendar year that exceeds two hundred million dollars  
7 (\$200,000,000) of purchases of qualified tangible personal property  
8 for which an exemption is claimed by a qualified person under  
9 this section. For purposes of this subparagraph, in the case of a  
10 qualified person that is required to be included in a combined report  
11 under Section 25101 or authorized to be included in a combined  
12 report under Section 25101.15, the aggregate of all purchases of  
13 qualified personal property for which an exemption is claimed  
14 pursuant to this section by all persons that are required or  
15 authorized to be included in a combined report shall not exceed  
16 two hundred million dollars (\$200,000,000) in any calendar year.

17 (B) The sale or storage, use, or other consumption of property  
18 that, within one year from the date of purchase, is removed from  
19 California, converted from an exempt use under subdivision (a)  
20 to some other use not qualifying for exemption, or used in a manner  
21 not qualifying for exemption.

22 (2) If a purchaser certifies in writing to the seller that the tangible  
23 personal property purchased without payment of the tax will be  
24 used in a manner entitling the seller to regard the gross receipts  
25 from the sale as exempt from the sales tax, and the purchase  
26 exceeds the two-hundred-million-dollar (\$200,000,000) limitation  
27 described in subparagraph (A) of paragraph (1), or within one year  
28 from the date of purchase, the purchaser removes that property  
29 from California, converts that property for use in a manner not  
30 qualifying for the exemption, or uses that property in a manner  
31 not qualifying for the exemption, the purchaser shall be liable for  
32 payment of sales tax, with applicable interest, as if the purchaser  
33 were a retailer making a retail sale of the tangible personal property  
34 at the time the tangible personal property is so purchased, removed,  
35 converted, or used, and the cost of the tangible personal property  
36 to the purchaser shall be deemed the gross receipts from that retail  
37 sale.

38 (f) This section shall apply to leases of qualified tangible  
39 personal property classified as “continuing sales” and “continuing  
40 purchases” in accordance with Sections 6006.1 and 6010.1. The

1 exemption established by this section shall apply to the rentals  
2 payable pursuant to the lease, provided the lessee is a qualified  
3 person and the tangible personal property is used in an activity  
4 described in subdivision (a).

5 (g) (1) Upon the effective date of this section, the Department  
6 of Finance shall estimate the total dollar amount of exemptions  
7 that will be taken for each calendar year, or any portion thereof,  
8 for which this section provides an exemption.

9 (2) No later than each March 1 next following a calendar year  
10 for which this section provides an exemption, the board shall  
11 provide to the Joint Legislative Budget Committee a report of the  
12 total dollar amount of exemptions taken under this section for the  
13 immediately preceding calendar year. The report shall compare  
14 the total dollar amount of exemptions taken under this section for  
15 that calendar year with the department's estimate for that same  
16 calendar year. If that total dollar amount taken is less than the  
17 estimate for that calendar year, the report shall identify options for  
18 increasing exemptions taken so as to meet estimated amounts.

19 ~~(h) This section is repealed on January 1, 2023.~~

20 *SEC. 2. This act provides for a tax levy within the meaning of*  
21 *Article IV of the Constitution and shall go into immediate effect.*

22 ~~SECTION 1. It is the intent of the Legislature to develop a new~~  
23 ~~economic program that would operate in areas with high~~  
24 ~~unemployment.~~